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### Labour migration and substitution (updated)

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## **INT-AR Paper 3<sup>i</sup> – Labour migration and substitution – Jan Cremers (UvT)**

### **What is substitution on the labour market?**

This (revised) paper compares the outcomes of several national and international studies on substitution as a consequence of migrants entering the labour market. Substitution appears if finding a job by one person results in the job loss (or non-obtaining of a job) of another person. The notion has been defined in different manners. One form of substitution is the use of social benefit earners for unpaid work, resulting in the disappearance of comparable paid work. Another form is the disproportionate and excessive utilisation of trainees or the transferring of paid work to volunteer work, for instance in the public sector. Labour market experts qualify a situation where unemployed work below their skill level a form of conjunctural or cyclical substitution: in period of economic downturn and increasing unemployment the supply of labour is larger than the available employment. Employers have the opportunity in such situations to come up with higher demands and recruit highly skilled persons that will substitute lower skilled workers.

Although labour migration regularly leads to a situation where there is a mismatch between the (high) skill level of the recruited foreign workers and the offered jobs, this phenomenon is not conceived as cyclical substitution. Substitution related to labour migration (here widely understood, both as labour mobility of EU-citizens and labour migration by 3<sup>rd</sup> country workers) is most often used as a more elegant wording of ‘they take our jobs’. In the search for the reduction of labour costs employees are recruited who demand less and are flexible employable.<sup>ii</sup> There is substitution if the decrease of jobs for the local residents is an evincible consequence of the entering of labour migrants. The Dutch social-economic council (SER) distinguishes in its labour migration advice between direct substitution (job losses as a result of a job taken by a migrant) and indirect substitution (inland supply has less changes as a result of the existence of foreign supply).<sup>iii</sup> The SER-advice on labour migration resumes that most available studies (at macro level) indicate low substitution effects, even in times of crisis. According to the SER, the outlook can be different if certain occupations or branches are analysed.

### **Research of substitution before the economic crisis**

Several research projects have focused on the possible substitution effects of labour migration and mobility. In one SEO-project dedicated to the economic effects, for the period 1999-2005, there was no evidence of large-scale substitution or displacement of residents after the arrival of long-term staying labour migrants from CEE-countries. The growing entering of long term staying labour migrants had by contrast a positive effect on the domestic employment. Temporary migrants indeed – probably because they were cheaper – substituted to a limited degree the workforce already present. Ultimately, the influx of labour migrants had a (slight) downward effect on the average wage level. This effect was limited to the lowest wage levels and completely absent in the higher levels. For the lowest wage earners, a high share of labour migrants in a sector and region entailed a negative downward pressure on their wages.<sup>iv</sup>

In a follow-up, the effect of the presence on the market of labour migrants after 2005 has been analysed.<sup>v</sup> According to the researchers, the influx of long-term residing labour migrants from CEE-countries in the period 1999-2008 had no significant net effect on the overall total of jobs for Dutch employees. It seemed that the labour market easily could handle this additional supply of workers. The researchers found positive effects in growth segments of the market: the supply of foreign workers supplemented the inland supply. Negative effects were registered in declining parts of the market: labour migrants competed with domestic supply. The effects in both parts of the market were so minor that the outcome in the end was zero. Though the supply of foreign workers doubled in the period 2005-2008, the labour market was not characterised by a substitution of Dutch workers.

The results correspond with the outcome of British studies for the period 1997-2005, a period that labour migration to the UK increased substantially. These studies hardly found any substitution of employment; but there was a downward pressure on low wages (and a positive effect for higher wage groups of workers).<sup>vi</sup> In the UK, this resulted, first and foremost, in a downward pressure on the wages of migrants already present on the market. Labour migration had no significant effect on the employment perspective of British workers. The Migration Advisory Committee (MAC) of the British government came up with another link between pay and the inland supply. In short, this governmental advisory body claimed that an improvement of the lowest wages in some sectors could serve as a strong incentive for the enlisting of British workers: 'Without upward pressure on wages there is little incentive for more natives to enter these occupations and the reliance on migrant labour will be a permanent rather than temporary feature of these labour markets'.<sup>vii</sup> Economic analysis in Norway presented similar outcomes: the supply of migrant labour creates a downward pressure on the lowest wage scales. There is an indirect substitution effect. However, in times of economic booming these effects are not perceptible because society at large profits of the presence of migrant labour.

Research on substitution at the Dutch labour market, commissioned by the ministry of labour, led (at the end of 2014) to the conclusion that workers in some sectors were exposed to substitution as a result of the influx of foreign labour from CEE-countries. The main argument was unfair, distorted competition, partly based on EU-regulations. It is cheaper for employers to hire staff from abroad through the use of fake agencies, letterbox companies or other middlemen. The main risks groups that suffer from substitution are the low-skilled, youngsters and migrants that are already present. However, migrants that enter the Dutch labour market particularly take up jobs and tasks that are neither aspired nor accepted by Dutch unemployed.<sup>viii</sup>

### **Substitution during the economic crisis**

Most recent studies don't provide evidence of a link between the presence of migrant labour from CEE-countries and the domestic employment during the crisis. Researchers expect migrant labour to be mobile and to disappear as soon as the employment outlook becomes worse; an effect that is strengthened by a restrictive access to social security benefit in most host countries. In the study, commissioned by the Dutch labour ministry, research institute SEO found out that labour migration from Western European countries decreased, however, migration from Eastern Europe did not change. In the agricultural, the manufacture, the construction, the retail and the transport sectors the total employment of Dutch workers decreased with digit percentages, combined with an increase of foreign labour. The jobs were most often shifted from direct labour into temporary and flexible contracts. In these sectors the search for cheap labour was combined with an ongoing process of flexibilization. The cost reduction was achieved through the recruitment of labour migrants who accept lower wages and high flexibility. This type of substitution mainly took place in labour-intensive jobs with standardised work, with a calculation and a competition based on price, not on quality, and in situations where language skills are neither essential, nor important.<sup>ix</sup>

SEO concluded that employees in sectors with a high participation of migrant workers did not end up in unemployment or inactivity at a massive scale. New entrants and job seekers are no subject to competition in the search for a job. The dynamic on the labour market explains why on average the development of inactivity in sectors with a large contingent of labour migrants does not deviate compared with sectors that have a low volume of migrant workers. Labour migration has a distributional effect on certain categories of workers. These effects are both negative and positive. Some high-risk groups that have to compete with migrants are confronted with negative effects. Other categories hardly have to compete and encounter positive effects.<sup>x</sup>

### **Recent findings on labour market effects**

In a majority of analyses substitution is assessed from the perspective of job losses and direct and indirect employment effects. However, this is only a part of the story. Another aspect is often neglected, that is the effect on the flexibilization of the labour market. The impact of the recruitment of migrant workers is probably stronger with regard to this indirect influence. It has to be said that there is a longstanding shift from direct labour towards flexible contracts among the Dutch labour population, notably in the services, construction and transport sectors. However, the recruitment of labour migrants, as several sources indicate,

is almost exclusively through flexible, temporary and short-term labour contracts, thus further facilitating the externalisation and flexibilization of the labour market.<sup>xi</sup>

Research in France, dedicated to the impact of immigration on the wages and employment of similarly skilled native workers, confirms this assumption from another angle. The author decomposes the population of native workers by job contract to investigate how job contract (and therefore wage rigidity) can protect the labour market outcomes of natives from immigration. He concludes that immigration has no wage impact on the population of native workers under indefinite-term contracts, whereas it reduces the wages of the native population under fixed-term contracts. This asymmetric wage impact indicates that the wages of workers under fixed-term contracts can be manipulated by firms to adjust labour cost. Since fixed-term contracts have a short duration and they terminate at no cost, they provide firms with a scope for wage adjustment: firms hire the new employees at lower wages than those who terminated their fixed-term contracts. The labour turnover on indefinite-term contracts is lower, particularly because most hiring occurs on fixed-term contracts. Workers choose not to change their direct job for a temporary job in another company. In addition, workers on indefinite-term contracts tend to be more protected. As a result, firms are unable to lower the wage of the native population covered by indefinite-term contracts. While indefinite-term contracts exert a protective effect on wages, an increase in the number of migrants decreases the employment level of native workers under indefinite-term contracts. Firms use the exit of native workers under indefinite-term contracts to replace them by migrants.<sup>xii</sup>

If this is combined with a lowering of the working conditions and pay, the increase of migrant labour will negatively influence the share of direct labour on the labour market. Whilst direct labour protects the working conditions and pay, a growth of migrant labour thus threatens the stable form of labour relations of workers in direct labour. There is no loss of employment as such, but a slow and advancing reduction of secured jobs and stable labour relations.

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<sup>i</sup> Second, revised version, January 2017.

<sup>ii</sup> The next citation indicates that these workers are not only coming from CEE-countries: 'British workers are more motivated and willing to work hard (...). The reason is that you don't have to contribute to a sickness insurance in England and there is no mandatory pension pay if they come on a temporary basis. Besides, the contract structure in Britain leads to an income tax of 20% whilst in the Netherlands income taxation is one quarter of your wage'.

<http://charlottedet.plazilla.com/page/4294999891/verdringing-op-de-arbeidsmarkt>

<sup>iii</sup> However, this distinction is not applied in the remaining of the SER-analysis (SER, 2014, Arbeidsmigratie, Advice 14/09).

<sup>iv</sup> De economische impact van arbeidsmigratie uit de MOE-landen, Bulgarije en Roemenië (The economic impact of labour migration from CEE-countries, Bulgaria and Romania), SEO, Amsterdam, 2008

<sup>v</sup> De economische impact van arbeidsmigratie: verdringingseffecten 1999-2008 (The economic impact of labour migration: substitution effects 1999-2008), SEO, Amsterdam, 2011.

<sup>vi</sup> [http://www.migrationobservatory.ox.ac.uk/sites/files/migobs/Briefing%20-%20Labour%20Market%20Effects%20of%20Immigration\\_0.pdf](http://www.migrationobservatory.ox.ac.uk/sites/files/migobs/Briefing%20-%20Labour%20Market%20Effects%20of%20Immigration_0.pdf)

<sup>vii</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/452805/Review\\_of\\_Tier\\_2\\_-\\_Analysis\\_of\\_salary\\_thresholds.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/452805/Review_of_Tier_2_-_Analysis_of_salary_thresholds.pdf), page 103.

<sup>viii</sup> <http://www.nu.nl/politiek/3924694/asscher-niet-bang-meer-verdringing-arbeidsmarkt.html>

<sup>ix</sup> According to the statistical office CBS, 75% of the registered Polish workers in the Netherlands work for a temporary work agency. The other quarter is active in agriculture (12%), retail and manufacture. A study by the employers' organisation ABU on 'flexmigrants' revealed that 30% of all flexmigrants works in logistics (and distribution), 30% in agro- and horticulture and 25% in the food industry. Metal scores 7% and all other sectors score below 2% (ConclusR Research, 2014).

<sup>x</sup> Grensoverschrijdend aanbod van personeel (Cross-border supply of personnel), SEO, Amsterdam, 2014.

<sup>xi</sup> See for instance: Damian Raess & Brian Burgoon, Flexible Work and Immigration in Europe. British Journal of Industrial Relations, 2015, 53:1. The authors analyse the impact of labour migration on the labour market based on a dataset in 16 countries. <http://onlinelibrary.wiley.com/doi/10.1111/bjir.12022/pdf>

<sup>xii</sup> Anthony Edo, How do rigid labor markets absorb immigration? Evidence from France. IZA Journal of Migration 2016, 5:7. <http://izajom.springeropen.com/articles/10.1186/s40176-016-0055-1#Sec15>